

Competing on Compliance – Building a Competitive Saudi Financial System for the 21st Century

Remarks by Mike Mannina, U.S. Treasury Attaché to Saudi Arabia at
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Introduction

Sabah al-Khair, salaam alekum. I'd like to thank the Saudi Banking Institute, SAMA, and Thomson Reuters for organizing this event and inviting me back to speak for a second time. As the U.S. Treasury Department's head of our Saudi Arabian mission, I regularly speak with bankers and government officials from around Saudi, the Gulf, Europe and the United States. I'm always curious to know how they view current AML-CFT trends and the broader state of regulatory reform on the global scale and how they view Saudi Arabia. Today I want to share with you a few observations I've learned from those conversations and offer suggestions as to how to make Saudi Arabia a highly competitive financial system for the 21st Century.

Past Saudi Success

There is no doubt the Saudi Banking sector has been a great success story. You have a strong Central Bank with good leadership at SAMA, your banks have earned some of the highest margins globally, and you were one of the first Basel III compliant jurisdictions.

Furthermore, the Saudi economy has been growing, your government's fiscal position is strong, and Fitch just upgraded the Kingdom's credit rating to AA.

Within the Saudi economy, the financial sector has seen one of the highest rates of *Saudization* and has done an excellent job *integrating women* into the professional workplace.

For these things I say, "Mabruk"! Today you are in a position of strength.

Past Performance Does Not Guarantee Future Success

But as every investor, unfortunately, knows all too well, "*Past Performance does not guarantee future success.*" This has never been truer than in today's rapidly changing financial world replete with new regulations, new threats, and interconnectivity like never before—and financial institutions worldwide must either quickly adapt or be left behind. No country or institution is exempt.

According to a large consultancy's latest Global AML Survey of banks worldwide, 84 percent of banker respondents listed the regulatory environment as their top AML focus for 2014 and indicated that the pace and impact of regulatory changes pose significant challenges to their operations. I suspect that if you're in this room today, you're feeling similar challenges.

But here's the new reality. While compliance has always been important, we are in an era where *compliance is king*. And your institution's reputation—based on compliance—is your greatest asset.

My message this morning is simple: *Compliance today – Profits tomorrow.*

This holds true for banks and jurisdictions—whether they be the United States, the UK, the UAE, Turkey, Saudi Arabia or anywhere. Banks with the best compliance programs today will be the most profitable tomorrow.

To explain my case, I'll first discuss the current regulatory environment and how we got here. Then I'll address what this means for the Kingdom.

The Regulatory Environment Today:

If any of you were in Dubai last month at the Thomson Reuters GCC Regulators conference, you would have heard Jeff Singer of the Dubai International Financial Center say that regulators are the new “rock stars.” What I think he meant was that regulators have a new sort of “star” power—an ability to redefine the rules of how business is conducted. And so, there are new rules, new penalties for violating the rules and vigorous enforcement taking place worldwide.

Today's conference agenda give you a decent sampling of that new regulation: European Market Infrastructure Regulation (EMIR), Dodd-Frank, FATCA, Corporate Governance, fraud prevention and “Know Your Customer challenges. I'd add to that Basel III, the Volcker Rule, new Financial Action Task Force (FATF) methodology and new rounds of peer evaluations, and record-breaking enforcement penalties levied on major global institutions.

So, How Did We Get Here?

The current climate did not come about overnight. Rather, it was wrought after a collective breakdown of markets, institutions, and oversight that allowed unprecedented terrorist attacks, a massive global recession, and the near collapse of one of the world's largest currencies--all in roughly a decade. In response, governments acted to safeguard the financial system from repeating history.

Specifically, in response to terrorist attacks, governments strengthened global AML-CFT standards through the FATF, created new sanctions regimes, and created new tools to root out illicit financial abuse of the global financial system.

After the financial crisis of 2008 and the subsequent European debt crisis, the G-20 and others took action to ensure systemically important financial institutions were not taking undue risks, were better capitalized, and would not place costs of their poor judgment on taxpayers. Soon thereafter regulators and supervisors had been fully re-energized and began a series of actions to ensure that financial institutions were held accountable for not complying adequately with laws and regulations.

This trend is here to Stay

I believe this trend is here to stay. For we now all realize that in an interconnected system, it only takes one weak link to make the entire system vulnerable. Therefore, effective compliance has become basic requirement for doing business. And institutions are either doing compliance right or they are not.

Gone are the days whereby a bank in a G-20 country can brush aside global standards assuming

that because it is a “local” bank. For if it has a single foreign correspondent--or a domestic correspondent with a foreign correspondent relationship-- it is part of the global system.

I believe that in general, banks generally are getting the message.

According to same Global AML Survey, banks on average spend over 50 percent more on compliance and control functions than they did three years ago. While amount of money spent does not guarantee good compliance, it is a sign that bank leadership is taking the issue seriously enough to devote resources to address the problem.

The Competition of Compliance

While this is a global trend that you cannot avoid, there is plenty of room to capitalize on this opportunity. While you as a financial institution will always compete on product selection and treasury returns, you are now also in a *competition of compliance*. And while all institutions will eventually have to comply, those that succeed on compliance soonest will be best poised for growth in the coming years.

Ultimately, your reputation matters. The great prophet of the holy scriptures, King David (pbuh), once said *“A good name is more desirable than great riches—to be esteemed is better than silver or gold.”*

While that’s a mantra I live by personally, it is extremely applicable in today’s financial world where your reputation is your top commodity. A good reputation will over time bring you strong correspondents; which in turn offers you new business lines, new customers, and new profits.

Conversely, inadequate compliance will eventually tarnish your reputation. It will shut you out of correspondent relationships, force you to close down business lines, and could put you out of business. Furthermore, the cost of repairing a damaged reputation--if even possible-- is far more expensive than maintaining an already good name.

Recent press reports show many large financial institutions are reevaluating their global footprint and are exiting relationships that they deem too risky or that they do not understand. I predict that trend will continue for some time. Institutions and jurisdictions must get ahead of this trend and remove any perceived risk. And the best time to bolster compliance and your reputation is from a position of strength.

What does this all mean for Saudi Arabia?

For Saudi Arabia, today is your position of strength. As I highlighted in my opening remarks, your financial sector is strong on capital, strong on liquidity, and strong on profitability. That’s a great position that most Western institutions wish they were in.

But let’s face it, as my Saudi interlocutors remind me, you live in a rough neighborhood. There’s instability, war, and illicit activity all around you. It may not be your fault, but it is a *reality*.

So, your challenge is to demonstrate above and beyond that: 1) You’re safe to do business with; 2) That you know your customers wholeheartedly; and 3) that you’re doing everything you can to protect your system from abuse by money launders and terrorist financiers.

After working with so many of you for the past two years, I know you're making good progress, so keep advancing.

But remember, it is far easier to address deficiencies from a position of strength.

Get compliance right today, and beat your competition.

Get compliance right today, and watch the Tadawul grow tomorrow.

Get compliance right today and bolster the Kingdom's broader reputation and influence in the global financial space.

Compliance today. Profits tomorrow.